

GOVERNMENT OF INDIA



ADMINISTRATIVE REFORMS COMMISSION

REPORT

ON

CENTRAL DIRECT TAXES ADMINISTRATION

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CHAIRMAN

ADMINISTRATIVE REFORMS COMMISSION
GOVERNMENT OF INDIA
CAMP : 'KENGAL KRUPA', BANGALORE-6

January 6, 1969

My dear Prime Minister,

I have pleasure in presenting to you the Commission's report on Direct Taxes Administration.

2. The Commission had appointed a Working Group under the Chairmanship of Shri Mahavir Tyagi to study and report upon Direct Taxes Administration. I would like to record our appreciation of the valuable work done by the Working Group.

3. Direct Taxes which play a vital role in achieving the socio-economic goals of the nation constitute a very important area of Central Administration. In this report, we have devoted attention mainly to the administration of the tax system rather than to the subject matter of taxation.

4. The knotty problem which confronts the Income-tax Department is the growth of arrears of assessment and collections. We have, therefore, started with recommendations which seek to liquidate the arrears as early as possible and to prevent their further accumulation. The strategy proposed is to adopt summary methods of disposal of the small income cases and to devote better attention to the bigger ones. A new method has been proposed in this connection. It is to arrive at a prior agreement relating to the assessment for three years at a time in cases which involve very small business incomes. For cases involving higher incomes, simplification of law and procedure have been suggested, so that they could be disposed of at a quicker pace than at present. Dealing with uncollected demands, we have drawn attention to demands which are clearly irrecoverable and suggested a programme of an expeditious write-off of such demands on the basis of recommendations of reviewing bodies which include senior officers. We have also recommended that the recovery work which is now being carried on in many of the States by the State Governments be transferred to the Income-tax Department itself. We have pointed out the need for senior Officers impressing on the assessing authorities that they should not resort to unrealistically high demands in the belief that it will be creditable to do so. Such demands are an indication of lack of judgment and a sense of proportion, and lead to accumulation of uncollectable arrears.

5. Assesseees have to be helped rather than harassed. After all, they constitute a considerable section of our pay-masters. The hierarchy of officials have to work with a new spirit of helping and assisting them. Instructions may, if necessary, be issued to this effect. To help the assesseees, we have recommended the following facilities :

- (i) Publication of basic tax-literature simple and easily understandable; and
- (ii) opening of Collection counters in the Income-tax Offices themselves and maintenance of Personal Ledger accounts for the assesseees in the bigger cities.

6. Removal of avoidable complexities in law, which involve delay and vexation is another subject on which we bestowed consideration. The avoidance of an elaborate procedure for the registration of firms, the abolition of provisional assessments and the adoption of a standard "previous year" by Companies are some of the recommendations made. It has also been recommended that amendment to Tax Laws should be made only after providing adequate opportunities to all the interests concerned to express their views on the proposed amendments. In order that this purpose may be achieved, amendments should be made through separate Bills and not through the annual Finance Bill which requires to be passed in a hurry before a prescribed date.

7. The problem of evasion has also received our attention. In addition to providing severe punishment for the offence of evading taxes, it is necessary to build an effective system of collecting and disseminating information relevant for the purpose of making assessments. We have, therefore, recommended the strengthening of Special Investigation Branches and proper supervision of their working. We have also pointed out the need for external survey. Registration of all the assesseees in an All-India Register and the devising of a procedure for quoting the registered numbers in transactions involving capital transfers, or mercantile or banking transactions, exceeding in value a prescribed amount, have been recommended. Certain legislative measures have also been recommended to assist the Department in its attempts to deal with the problem of evasion. The law could be so amended as to compel a person to enter in his income-tax and wealth-tax returns, particulars of the assets or sources of income beneficially held for him. If such holdings are not declared in the tax return, no claims to them would be enforceable in law. Persons engaged in money-lending business (other than Banking Companies) should clearly indicate in the accounts of their business, money available for the business and keep in banks all amounts in excess by a maximum to be prescribed by law. Government should also be enabled by law to challenge transfer of immoveable property if, on the basis of expert advice, it is found to have been undervalued.

8. The Working Group's suggestion that the Central Board of Direct Taxes should be reconstituted as purely an executive authority without any responsibility for advising on policy was examined, and we came to the conclusion that it would be unrealistic to exclude the head of the Revenue Department from advising on policy. The Working Group's idea that Income-tax Officers on promotion to the cadre of Assistant Commissioners should receive training in Judicial practice and procedure for a small period could be accepted. This training should be a pre-condition to their appointment as Appellate Assistant Commissioners.

Yours sincerely

(sd.) K. Hanumanthaiya

Shrimati Indira Gandhi,
Prime Minister of India,
New Delhi.

CHAPTER I

INTRODUCTORY

Direct Taxes constitute one of the most important areas in the field of Central Administration. Besides bringing in a sizeable amount of revenue to the Government, they play a vital role in securing the national objective of so distributing the ownership and control of the material resources of the community as best to "subserve the common good". The principle of equity, conceived in the broadest sense, underlies the Direct Taxes structure. Thus Income-tax, the most important of the Direct Taxes, in its attempt to secure equity in the incidence of that tax takes into account the circumstances surrounding the emergence of the income subject to tax, e.g., whether it is earned by the unaided efforts of a single individual, or collectively through a firm or corporation; what outlay has been made in the shape of men, material and machinery. This inevitably leads to an elaboration of the substantive law relating to assessment. Again, equity requires that the income-tax burden on an individual be related to his ability to pay. This objective is sought to be achieved through a progressive rate structure, the incomes in the higher brackets bearing a rate of tax greater in proportion than to corresponding incomes in the lower brackets. Thus, the larger the income, the greater the tax incidence. This unfortunately leads to attempt at avoidance as well as evasion. Whether it is avoidance or evasion, the result on the society is just the same. The law has, therefore, from time to time, been further elaborated with a view to plugging loopholes and intensifying penal action against evaders. In this process of the elaboration of law, things are carried to such a length that quite a large number of assesseees who have comparatively smaller incomes are subjected to vexatious procedures based on various legal requirements without any significant advantage to revenue. Any refinements of law, in any case, have but little effect on the unscrupulous evader, who does not restrict himself to clever means to take advantage of loopholes in the law, but practices downright concealment.

2. Over the two decades there has been a plethora of amendments of the law relating to Income-tax. In 1961, the whole of the Income-tax Act was recast, the provisions arranged in a logical sequence, and an attempt was made to express the law in a language that could be understood without much difficulty. Hopes were expressed and assurances were given that the provisions of the law would remain stable for some time at least. However, in the years that followed, more than 400 amendments were introduced. The Administration naturally has been finding it difficult to keep pace with this incessant change in law. Further, the number of persons falling within the taxable category has progressively been increasing over the years as a consequence of the general rise in the tempo of economic activity in the country. In this context, the Income-tax Department is also handicapped by its cumbersome procedures based on considerations of technical nature. Consequently, there has accumulated a vast amount of arrears. There is also a general deterioration in public relations.

3. There is no doubt that the tax law affects intimately a vast number of citizens whose contribution to national wealth and national enterprises

of different types is of importance to national well-being. While it is necessary that, on the one side, loophole of avoidance are closed and concealment of incomes is dealt with drastically, it is equally important that, on the other, the honest citizen—and he is in a larger majority—is not unduly harassed by being required to comply with procedures irksome and irritating to the point of becoming disincentives. This important psychological factor so necessary to secure public cooperation in the enforcement of the income-tax and other direct taxation laws deserves particular attention.

4. The Commission decided to examine the functioning of the Direct Taxes Administration keeping in mind the factors set forth above. We did not think of going into details of substantive law relating to direct taxation. Our objective was a more limited one, namely, one of examining the law and procedures from the point of view of smooth administration and improvement of assessee-department relations. Accordingly, we set up a Working Group with the following limited terms of reference :

- (i) examine the machinery for the assessment and collection of the Central Direct Taxes and make recommendations with a view to achieving greater speed in completion of assessments and collection of taxes and greater efficiency in tackling tax evasion;
- (ii) examining the procedures which assessees and departmental officers are required to comply with and suggest modifications thereof with a view to eliminating avoidable inconvenience to assessees and unproductive labour for the administration; and
- (iii) locate the situations in which needless complexities are created in the administration of the tax laws and make suggestions for removing them.

The Chairman of the Working Group was Shri Mahavir Tyagi, a former Minister of Revenue and Expenditure in the Union Government and the Chairman of the Direct Taxes Administration Enquiry Committee of 1948-49. Other members were Shri S. N. Dwivedi, M.P., Shri S. A. L. Narayana Row, Chairman, Central Board of Direct Taxes, Shri R. N. Jain, then Director of Inspection (Investigation) and now Member, C.B.R., and Shri V. Gauri Shanker, Director of Revenue Audit, acting as Secretary of the Group. We would like to record our appreciation of the work done by the Working Group which has made a study of the various problems arising from direct taxes administration and has submitted a useful report.

5. As already stated, income-tax is the most important of the direct taxes and all the direct taxes are administered by the Income-tax Department. The Working Group has, therefore, appropriately concentrated on this tax and we have also done likewise.

6. In this report, we propose to consider only a few basic issues concerned mainly with the administration of the tax system and not with the details of the law relating to the subject matter of taxation. Thus, we shall deal with the disposal of the cases involving small incomes which have accumulated to an alarmingly large number, the prevention of such accumulation in future, the problem of collecting arrears of tax, assistance to assessees, removal of avoidable complexities in procedural law which contribute to delay and irritation, and the problem of tax evasion. We shall also deal with some questions of administrative reorganisation.

7. Government have already taken action on the following matters on lines which are in agreement with the suggestions of the Group :

Item No. in summary of the Group's recommendations.	Subject	Reference to provisions in the Act or Rules
12	Curtailling the time limit for making assessments.	Section 153(1) of the Income-tax Act, 1961.
76	Tax paid by a firm to be allowed as a deduction in the hands of the partners.	Section 67(1)(a) of the Income-Tax Act 1961.
86	Deduction of items of expenditure not relating to the construction and maintenance of property.	Section 24(iii) of the Income-tax Act, 1961, deleted and 24(iv) amended by Finance Act, 1968.
99	Abolition of the distinction between earned and unearned incomes for the purpose of tax and the abolition of surcharge on incomes above a lakh of rupees.	Finance Act, 1968.
100	Dropping of the Annuity Deposit Scheme.	Finance Act, 1968.
106	Penalty to be determined with reference to the income concealed.	Sec. 27(i)(iii) as amended by Finance Act, 1968

8. As mentioned above, we have bestowed consideration mainly to the problems of administration of the tax system. We have, therefore, not expressed an opinion on several of the suggestions of the Group including the ones relating to scales of pay. Alterations in the scales of pay is a delicate task and is apt to set chain reactions in other Departments of Government. Financial implications have to be assessed in detail before matters relating to pay scales can be decided upon. We, therefore, leave such matters to the Government for consideration in the wider context of the pay scales of Government servants in general. We have, however, drawn attention to an existing anomaly in the case of Assistant Commissioners of Income-tax and suggested rectification.

CHAPTER II

MEASURES TO EXPEDITE THE DISPOSAL OF ASSESSMENTS

Small income cases i.e., cases involving income not exceeding Rs. 10,000/-

Over the past eight years, there has been a steady increase in the number of assessments pending at the end of every year. Naturally, this has caused concern all round.

2. Making an analysis of the cases that require disposal, the Working Group has come to the conclusion that a very large percentage of them could be regarded as unimportant from the point of view of revenue and as not requiring much scrutiny. The Group has, therefore, suggested that the effort and attention devoted to these unimportant cases should be minimised so that better attention could be devoted to the cases involving higher incomes.

3. The Group has, in this connection, examined a suggestion that the number of small cases could considerably be reduced by raising the maximum limit of income which is exempt from tax. It has come to the conclusion that though the suggestion looks attractive, it will create more problems than what it expects to solve. We agree with the Group's approach, particularly, where it refers to the need in a democratic set-up for citizens to feel that they have directly contributed to the Exchequer. We also agree with the Group's view that a pervasive tax consciousness is necessary for building up a healthy attitude against tax evasion.

4. The Group has suggested a system of compounded levy in the case of small shop-keepers, hawkers and vendors, most of whom do not maintain accounts. The formal process of annual assessment with all its procedural requirements is hardly worthwhile in their case. Considerable time and energy may be saved by adopting a system whereby the tax for the next, say, three years is fixed on the basis of the results of the last three assessments (or on the basis of the current assessment made on a new assessee). The Group has suggested that this scheme should be applied only to marginal taxable income and after adopting suitable safeguards. It should be applied only to cases of business in which the capital investment does not exceed Rs. 20,000/- The agreed levy should be operative only for a period of three years. At the end of the three years the assessee should file a statement of assets and return of income, and if on a scrutiny of his return of income and assets, he is found to be eligible for renewal of scheme, it can be extended for another three years. The incomes should be divided into a few groups, and the tax should be the same for all falling within any particular group. Suitable safeguards against misuse of the scheme by those who are not entitled to it could be devised.

5. Though the Commission would not in principle agree to a system of compounding in general, they consider a scheme of assessment based on prior agreement on the lines proposed by the Group worthy of trial in the case of persons with very small taxable incomes, who are not likely to maintain detailed accounts, e.g., small shop-keepers, hawkers and vendors. This method should apply only to marginal cases, say, where the taxable income is estimated not to exceed Rs. 7,500/- This method will, of course, provide only a means of preventing the future accumulation

of cases involving very small income but will not solve the problem of arrears which have already accumulated. Further, the scheme will require a careful study of the procedural mechanics involved and it may take some time before it is given a start. Meanwhile, we recommend for adoption a method of dealing with small cases, which, while expediting their disposal, will not create a serious risk to revenue. The method we recommend in this connection will involve a simple amendment of the law to enable the Income-tax Department to make summary assessments on the basis of incomes returned by adding back amounts clearly necessary for rectifying the apparent deficiencies noticed in the return. Under the law, as it stands today, it will be necessary to summon the assessee and discuss the amount with him before even obvious deficiencies are rectified. The law may be amended rendering it unnecessary to call the assessee for an interview if a small addition is made to the income declared in the return, in order to rectify deficiencies. A maximum may be fixed for the amount which can be so added without giving the assessee a hearing. If the law is amended as recommended above, the small income cases—a category in which we could place cases involving incomes not exceeding Rs. 10,000/- can be disposed of expeditiously. Such cases may be given a special marking so that they can quickly be picked up and disposed of. (The amendment to law proposed above may also apply to all cases, irrespective of the income, provided that the addition made is kept within a prescribed maximum. This will enable even bigger cases to be disposed of expeditiously if the returned income can be accepted with small additions. The assessee will, of course, be entitled to an appeal in any case).

6. After the arrears of small cases are brought under control, only a percentage of them need in future be subjected to a complete check after calling for the necessary information. This procedure will then form the normal method of dealing small cases. Meanwhile, the 'prior-agreement' method will have been introduced for dealing with very small business cases, i.e., those involving incomes less than Rs. 7,500/-. Assessment of salary and property incomes should not present any difficulties and they may also be expeditiously disposed of if the amendment proposed above is carried out.

Cases involving incomes over Rs. 10,000/- but not exceeding Rs. 50,000/-.

7. Cases involving incomes exceeding Rs. 10,000 are divided by the Group into two categories, namely, those with incomes not exceeding Rs. 50,000/- and those with incomes exceeding that amount. In this section, we deal with the former type of cases for which the Group has suggested the following procedure.

8. Where returns are prepared by authorised representatives and are duly supported by reports required to be given by them, the returns may be accepted on the basis of those reports, if they are found to be adequate. The assessment may then be completed without calling the assessee. It is only when the reports of the authorised representatives are considered inadequate for the purpose of accepting the returns as filed, that the usual procedure of calling further information and giving a personal interview to the assessee should be gone through. Where returns are not prepared by the authorised representatives, the full procedure of assessment should be gone through in the case of new assessee. In the case of the assessee, who are already on the list and whose record during the last three years has been unblemished, the returns may be accepted in 75%

of the cases and only 25% of them need be subjected to check. The checking should include (a) reconciliation of the income declared with the accumulation of wealth and the out-go including gifts during the relevant period; (b) checking of cash credits; and (c) quantitative reconciliation of the closing stock with the opening stock and checking of the valuation of the closing stock. Cases not covered by the categories described above will, of course, have to be disposed of after following the full assessment procedure. The Group has also suggested that the assessee should be required to file certain certificates regarding the correctness of the account books maintained by them.

9. We agree with the Group's proposals. We would add that the amendment to law which we have recommended in para 5 will enable the Income-tax Department to complete the assessments without calling the assessee when only minor add-backs are made.

Cases involving incomes exceeding Rs. 50,000/-.

10. The Working Group has suggested that for cases of incomes above Rs. 50,000/- there should be a hundred per cent check and that they must be compulsorily audited by Chartered Accountants who should append a complete list of points examined by them. It is further suggested that the more important of these cases should be assessed by the Inspecting Assistant Commissioner.

11. The question of compulsory audit of accounts had come up for examination on earlier occasions. The Income-tax Investigation Commission expressed itself in favour of compulsory audit in large income cases (para 2.05 of the report). The Direct Taxes Administration Enquiry Committee expressed the view that all cases of above Rs. 50,000/- should be compulsorily audited in the same manner as the accounts of the companies are audited under Section 227 of the Companies Act.

12. We agree that audit by qualified Chartered Accountants would be helpful in relieving the assessing authority of the need to make routine checks and enabling him to concentrate on the broader aspects of the determination of the assessee's correct liability. However, we are not sure whether audit made compulsory by law would not delay the submission of returns. Further, the number of Chartered Accountants being limited, it may not be possible for all assessee to secure their services except at heavy cost or at the cost of detailed scrutiny. The objective which the Group has in mind can be achieved if the provisions of rule 12—of the Income-tax Rules, 1962 are enforced after amending it to provide for the information as set out in para 2.16 of the Group's report. This would mean that a report containing the information required will be statutorily available only in a case where the return is prepared by Chartered Accountants. Such information will, of course, be necessary only where there is income exceeding Rs. 50,000/- from business.

Recommendation :

1

We recommend :

- (1) A system of prior agreement of the income-tax liability for the next three years, based on the results of the last three assessments (or on the basis of the current assessment made on a new assessee) may be introduced for

dealing with the cases of small shop-keepers, hawkers and vendors (who are not likely to maintain regular accounts) where annual incomes does not exceed Rs. 7,500/-.

- (2) The law may be amended rendering it unnecessary to call the assessee for an interview if a small addition is made to the income declared in the return in order to rectify deficiencies. The maximum of addition that can be so made may be fixed by law.
- (3) The procedure for assessment in cases other than those mentioned in (1) may be simplified in the manner described in paragraphs 7 to 9.
- (4) The provisions of Rule 12A may be amended so as to provide for the furnishing of the following information in all cases in which the returned income from business exceeds Rs. 50,000/-, and the returns are prepared by Chartered Accountants :
 - (a) a brief history of the case;
 - (b) the nature of the business;
 - (c) the books of account maintained;
 - (d) the documents sent along with the return;
 - (e) the number of bank accounts maintained;
 - (f) brief explanation of the various loans and overdrafts appearing in the Balance Sheet; and
 - (g) a brief explanation of the entries in the capital account.

CHAPTER III

ARREARS OF COLLECTION

One of the maladies from which the Income-tax Department is suffering is the rising trend of uncollected demands. The Group has mentioned the following factors as having contributed to the accumulation of the arrears :

- (a) Stay obtained by tax payers at the appellate stages;
- (b) Delayed and cumulative assessments made in big assessment cases resulting in large demands at a single point of time forcing the tax payer to ask for instalments;
- (c) Assessments being made after the assessees had become insolvent or companies had gone into liquidation;
- (d) Assesseees having left India for good mostly for Pakistan, leaving behind no assets; and
- (e) Assesseees not being traceable, or where traceable, having little or no assets to meet the demand raised against them.

We would add to the above list one more item, viz., unrealistic demands raised in several cases. Though the Group has not specifically mentioned this as one of the factors contributing to the accumulation of uncollected taxes, it was aware that allegations have been made of demands being pitched unrealistically high.

(i) Stay of collection in cases under appeal

2. Under the provisions of the Income-tax Act, the Income-tax Officer may, in his discretion, allow an assessee to defer payment of an amount of tax under dispute in an appeal before the Appellate Assistant Commissioner till the appeal is disposed of. No power has been given to the Income-tax Officer or to any other Income-tax authority to stay collection of tax when appeals are preferred to the Appellate Tribunal, the High Court or the Supreme Court. The Direct Taxes Administration Enquiry Committee which considered the question whether such an express power should be given to the authorities to stay collection of tax when appeals are preferred to the Appellate Tribunal or higher courts, expressed itself against such a provision on the ground that it would encourage assesseees to file frivolous appeals merely with a view to obtaining time for payment of tax and also on the ground that it would involve duplication of work of the appellate authorities who will have to deal with the cases twice, once when an application is made for stay of collection and again when the cases are heard on merits for disposal. In spite of the absence of the specific provision enabling the authorities to give extension of time, the prevalent trend of opinion appears to be that an appellate authority has an inherent jurisdiction to entertain positions for stay of tax in regard to matters on appeal. It would appear that the appellate authorities need not distinguish between the amount disputed in appeal and the undisputed amount. There is really no case for the postponement of the payment of tax on the income in respect of which there is no dispute.

3. We agree with the Working Group and recommend :

Recommendation

2

Appropriate amendment should be made in the Income-tax Act to provide that no appeal will be entertained from an assessee unless the tax on the undisputed amount involved in the assessment is paid or satisfactory arrangements are made for the payment of such tax.

(ii) Write-off of irrecoverable demands

4. The factors set forth in (c), (d) and (e) of para 1 and the unrealistic demands raised in several cases have led to large accumulation of arrears which, in fact, are irrecoverable. No useful purpose is secured by carrying in the books such irrecoverable arrears, which only create a misleading picture of the recoverable content of these arrears. The proper thing to do, in the circumstances, is to write off the irrecoverable demands. There is, however, a reluctance to write off demands—reluctance which is attributed by the Group to a fear among the Income-tax authorities that their action in writing off would be open to criticism in Parliament and elsewhere. This fear should be removed by an assurance that the write off of arrears clearly proved as irrecoverable is the proper thing to do and is not an act calling for criticism. We agree with the Group that write-off decisions may be taken by a Committee instead of by a single officer. For cases involving not more than Rs. 2 lakhs, the Committee may consist of the Commissioner, the Inspecting Assistant Commissioner and the Income-tax Officer. The write off of amounts ranging between Rs. 2 lakhs and Rs. 5 lakhs may be authorised by a Committee consisting of the Commissioner and a Director of Inspection. Where higher amounts are involved, the Committee consisting of the Commissioner and the Director of Inspection may put up the case for write off for the Board's approval.

Recommendation

3

We recommend :

Action should be taken for expediting the write off of outstanding demands if they are found clearly to be irrecoverable. Such demands should be scrutinised by a committee consisting of the Commissioner, the Inspecting Assistant Commissioner, and the Income-tax Officer concerned if the amount to be written off does not exceed Rs. 2 lakhs. Where such amount ranges between Rs. 2 lakhs and Rs. 5 lakhs, the Committee for scrutinising should consist of the Commissioner and a Director of Inspection. Where higher amounts are involved, the Commissioner and a Director of Inspection should scrutinise the cases and put them up to the Board for disposal.

5. In several cases, the full amount may not be recoverable, but only a part of it might be. In such cases, the demands are suitably scaled down on the recommendations of a Committee consisting of a Director of Inspection and the Commissioner as approved by the Board. The initiative in such cases comes from the assessee themselves and the terms of scaling down are incorporated in agreements with them. The Working Group considers that this procedure has been working satisfactorily. The only suggestion it makes in this connection is that the assessee should be required

to give an undertaking that if any assets not hitherto disclosed come to light, the settlement for the scaling down will fall through and the full demand will become enforceable. We are in agreement with this suggestion.

6. While the above suggestions deal with arrears which have already accumulated, it is necessary that future accumulations should be prevented by insisting on the timely completion of assessments and the avoidance of making demands out of tune with the facts of the cases involved. The Inspecting Assistant Commissioners and the Commissioners have an important role to play in this regard. It should be impressed by them that over-assessment would be counted as a defect indicating want of judgment and a sense of proportion in the assessing authority. They should also see to it that proper programmes of work are drawn up and adhered to, so that big cases are not left undecided for a long time.

Recommendation

4

We recommend :

Commissioners and Inspecting Assistant Commissioners should impress on the assessing officers that over-assessment would be noted as a defect indicating want of judgment and a sense of proportion.

(iii) Coercive processes for recovery

7. Enforcement of demands through coercive processes, in cases where payments are not made within the time prescribed, is, with some exceptions, done through State Revenue Officers. The Group has pointed out that this arrangement has been unsatisfactory. The Income-tax Act contains a full recovery code and provides for the taking over of the work relating to coercive recoveries. Yet it is only in Delhi, Rajasthan, M.P., Madras City, Gujarat and Mysore that this work has been taken over by the Income-tax Department. We agree with the Group that this work should fully be taken over by the Income-tax Department and that a target date should be fixed for the purpose.

8. The Group has referred to the absence in the Estate Duty Act of provisions for recovery of dues similar to those in the Income-tax Act, and has proposed an amendment to the Estate Duty Act for incorporating in it such provisions. It has also drawn attention to the need in the Estate Duty Act of a provision to prevent the transfer before payment of Estate Duty of immovable property left by a deceased intestate. We are in agreement with these proposals.

Recommendation

5

We recommend :

- (1) The recovery work should be taken over by the Income-tax Department in those charges where it is now entrusted to the States.**
- (2) (a) The Estate Duty Act may be amended so as to provide for recoveries on the lines provided in the Income-tax Act.**
(b) Provision may be made in the Estate Duty Act for the prevention of transfer, before payment of the relevant Estate Duty, of immovable property left by a deceased intestate.

CHAPTER IV

FACILITIES FOR TAX-PAYERS

Informative brochures

Income-tax proceedings consist broadly of four stages :

- (a) pre-assessment proceedings, such as payment of advance tax, and deduction of tax at source;
- (b) assessment proceedings beginning with the submission of returns followed by payment of self-assessment tax, compliance with various requirements in the course of the examination of accounts and ending with the determination of liability;
- (c) payment of the tax and the processes relating thereto;
- (d) appeal proceedings where appeals are preferred.

2. Each one of these stages involves compliance with various procedural requirements. However, the assistance given to the tax-payers in this connection by the Department is meagre. There have been sporadic attempts at publishing booklets, such as the "Income-tax for the Layman", "Estate Duty for the Layman" and an "Outline of Direct Taxes". But even these publications are now out of date. It is, therefore, necessary that basic literature on tax payers' obligations and rights should be brought out in Hindi, English and the regional languages. Such literature should include small brochures explaining particular aspects of the law and the rules on matters like the determination of liability of non-residents, determination of the liability of firms, Hindu Undivided Families, rebates and reliefs admissible, allowances like depreciation and development rebate. These brochures may be kept in a folder and made available to assessee free of charge or on payment of a small sum. This folder should also contain the forms of return of income and such other forms as are required to be filled by an assessee periodically, such as, estimates for advance tax. It should prominently set forth the various "due" dates which an assessee has to keep in mind for complying with the various provisions of the law.

Recommendation

6

Basic literature on tax-payers' obligations and rights should be brought out in Hindi, English and the regional languages.

Payment of tax in Income-tax Offices

3. The existing procedure for payment of tax dues into the local treasury or at the State Bank or at the Reserve Bank of India conducting the cash business on behalf of the Government is tortuous and has been a cause of annoyance to tax payers. Incidentally, it creates difficulties in reconciling the amounts actually paid into the treasury and the amounts as recorded in the departmental books. Under the present system, along with the demand notice, challans are issued in triplicate to the assessee to enable him to pay the tax into the treasury. The treasury or the State

Bank of India or the Reserve Bank of India, as the case may be, acknowledges the receipt of the money and issues one copy of the challan to the remitter retaining two copies. The Bank or the treasury sends the original part of the challan to the Income-tax Officer and the duplicate to the Accountant General. On receipt of these counterfoils, they are entered in a Daily Collection Register in the Income-tax Office. From the Daily Collection Register they are periodically posted in the Demand and Collection Register. The Daily Collection Register is sent to the treasury every month for verification of the departmental figures. There has always been difficulty in reconciling the figures as reported in the departmental books and as accounted for in the treasury. Further, as remarked by the Working Group, "the present system of maintaining the Demand and Collection Register does not enable the Revenue Department to find out the total dues outstanding against an assessee or refund due to an assessee at a glance of the register since arrears, current demands and collections are kept separately for each year in several folios of the Demand and Collection Register".

4. Having regard to these difficulties and the defects involved in the present system of collection of tax and payment of refunds, the Working Group has suggested a scheme under which cash counters will be operated in the Income-tax Department itself and an individual ledger account will be maintained for each assessee. The details of the scheme are given in paragraphs 4.9 to 4.12 of the Working Group's report.

5. The main advantage to assesseees of the scheme outlined by the Group is that their dues are realised right across the counter in the Income-tax Department itself. In so far as the Department is concerned, the personal ledger would enable the Department to keep a close watch on the demands due from or refunds due to the assessee. The correctness of the balance is secured by communicating it to each assessee and obtaining his confirmation at the close of the year. At a glance, one can find out the position of arrears in respect of demands and collections accurately and quickly.

6. However, the opening of personal ledger accounts for all the assesseees in India all at once would be too much of a burden. Further the difficulties associated with the payment of tax into the treasury or the bank and of the reconciliation of the figures are not so great in the mofussil places as in big cities.

Recommendation

7

We therefore recommend that the scheme regarding the opening of cash counters in Income-tax offices and the maintenance of Personal Ledger Accounts as suggested by the Working Group may be examined by the Government for being introduced in big cities like Bombay, Calcutta, Delhi, Madras, Kanpur, Bangalore, Ahmedabad and Hyderabad.

7. It is necessary that the assessing authorities should so conduct themselves that the assesseees can depend on them for assistance and guidance in complying with the requirements of law relating to assessment. The authorities should do their best to project before the tax-payers an image of a helpful guide rather than that of a rigid official indifferent to the difficulties of the assesseees.

REMOVAL OF AVOIDABLE COMPLEXITIES IN THE LAW

General

A major factor in proper tax compliance is a clear, unambiguous tax code, the provisions of which are not altered too often by amendments. It was hoped that when the Income-tax Act was thoroughly overhauled and a new enactment viz, the Income-tax Act, 1961, replaced the Act of 1922, there would be stability in the Income-tax law for some time. However, as pointed out by the Working Group, in the years that followed the passing of the Income-tax Act in 1961, more than 400 amendments have been made creating the confusion of the type which was sought to be removed by the Act of 1961. The first step in avoiding complexity is to minimise amendments and towards this end, we recommend that :

Recommendation**8**

- (a) Amendments to tax laws should be made only after a careful survey of their total effect by all concerned. It will not be possible to make such a survey if amendments are rushed through the annual Finance Bill which needs to be passed before a prescribed date. Such amendments should therefore be made through separate Bills whose provisions can be considered in detail by select committees and on which the various professional or trade and industrial bodies will have an opportunity to express their considered views.
- (b) Before rules are amended or new rules framed the views of the Commissioners of Income-tax and of leading professional or trade and industrial bodies should be ascertained and considered.

"Previous Year"

2. The Working Group has drawn attention to the complexity introduced by the provisions relating to the "previous year". Under the Income-tax Act, the tax is levied on the income earned in the "previous year" which is defined in Section 3 of the Act. Every assessee is in effect given the right to follow a separate "previous year" for each source of his income, the source sometimes meaning even a branch of a business. So an assessee can have for his various items of income a number of "previous years" ending on several dates falling within the previous financial year. This in itself creates complexity in assessment.

3. Further, the adoption of different "previous years" creates difficulties in the matter of verification of transactions between assesseees having such different previous years and for comparing their profit margins. There is also the difficulty in forecasting with reasonable accuracy budgetary receipts. The problem could be solved by prescribing a uniform standard previous year for all assesseees instead of permitting each of them to have his own "previous year" or years. However, it may not be practicable to insist upon the case of a standard "previous year" by all the assesseees who have for a very long time, been adopting different accounting years like

the Diwali year, the Samvat year etc. As a large part of the taxes comes from companies, which are comparatively small in number and as they are better equipped than other assesseees for effecting the changes required for adopting a new accounting year, we suggest that a standard previous year may be fixed only for companies. Most of the companies adopt either the calendar year or the year ending June for closing their accounts. The Working Group has expressed its preference for the calendar year.

4. The above suggestion has been made on the assumption that the fiscal year will remain the same as at present, viz., the year beginning from 1st April and ending on the 31st March following. However, the Administrative Reforms Commission had recommended to the Government in its report on "Finance, Accounts and Audit" that the commencing date of the fiscal year should be changed from the 1st of April to the 1st of November. If this suggestion is accepted, the standard previous year to be fixed for companies could more appropriately be the one which ends on 30th of June. However, if the present system of taking the financial year as beginning from the 1st of April is to continue the calendar year may be taken as the previous year.

Recommendation

9

We recommend :

A standard "previous year" should be prescribed for companies. This may be the calendar year if the financial year continues to commence on the 1st of April. However, if the financial year is to commence on the 1st of November as recommended by us in our report on "Finance, Accounts and Audit", the "previous year" for companies may be taken to be the year ending on the 30th of June.

Registration of firms

5. In the Income-tax Act, a distinction is made between registered firms and unregistered firms in regard to the determination of the tax liabilities of the firms and the partners. In the case of the partners of a registered firm, tax is levied on the basis of their shares of income from the firm. The registered firm also pays a tax depending on its income. This tax at present ranges between 6 and 12 per cent. An unregistered firm pays tax on its total income as if it were an individual at the rate applicable to that income. In the hands of the partners their shares from the firm are included in their total income only for the purpose of determining the effective rate of tax leviable on the rest of their income. Thus the fact that a firm is registered has an important bearing on tax liability of the firm and its partners. Rules have been framed providing for the submission of an application for reistration accompanied by an instrument of partnership setting out the shares of the partners and signed by all the partners. The processes prescribed for registering a firm under the Income-tax Act have often landed the assesseees and the Department in litigation mostly on technical grounds. So long as there are specific legal provisions prescribing the procedural requirements for getting the benefit of registration, disputes are bound to occur as to the fulfilment of these requirements notwithstanding the existing of a genuine firm.

6. The Working Group has suggested the conferment, as a general rule, of the benefits of registration to all firms which are constituted under

an instrument of partnership and registered with the Registrar of Firms under the Indian Partnership Act. We agree with the Group that there is no point in applying the word 'registered' to a firm when what, in fact, happens is to recognise its existence. The expression "registered firm" may therefore, be substituted by the expression "recognised firm". While accepting the suggestion of the Working Group, we consider it necessary to take precautions. The recognition of the firm should be subject to—

- (a) the partnership being evidenced by an instrument of partnership specifying the shares of partners;
- (b) the partnership being registered with the Registrar of Firms within six months of its commencement;
- (c) any change in the constitution of the firm being evidenced by a new partnership deed, registered with the Registrar of Firms;
- (d) none of the partners of the firm being a nominee or a benamdar in any other; and
- (e) the return of income of the firm being signed by all the partners.

There should be a provision for the cancellation of recognition if the partnership is found to be a bogus one.

7. Along with the liberalisation of the procedure for recognition of firms, a change in the manner of taxing such recognised firms is called for. At present a registered firm pays a tax on its total income at the following rates :

		Rs.	
Income not exceeding	. . .	25,000	Nil
Income exceeding	. . .	25,000	6% of the amount by which the total income exceeds Rs. 25,000.
but not exceeding	. . .	50,000	
Income exceeding	. . .	50,000	Rs. 1,500 plus 8% of the amount by which the total income exceeds Rs. 50,000.
but not exceeding	. . .	1,00,000	
Income exceeding	. . .	1 lakh	Rs. 5,500 plus 12% of the amount by which the total income exceeds Rs. 1 lakh.

This method of levy of tax on firms ignores the fact that the revenue advantage is dependent on the number of partners constituting the firm; the greater the number, the greater the revenue advantage. The Working Group has accordingly suggested that the tax must be levied on the registered firms on the basis of the number of partners and not on the basis of income.

8. For this purpose, it has recommended that the rates may be fixed as follows :

- (a) Partnerships with four or less partners . . . 10%
- (b) Partnerships with more than four partners but less than eight partners . . . 12½%
- (c) Partnerships with more than eight partners . . . 15%

9. We agree that it would be appropriate if the tax on a registered firm is prescribed with reference to the number of partners *i.e.*, the greater the number of partners the higher the rate of tax. However, we do not

propose to make any recommendations regarding the rates which will have to be fixed by the Government in the light of fiscal considerations.

Recommendation

10

We recommend :

- (1) Partnership may be recognised for the purpose of income-tax assessment if**
 - (a) it is evidenced by an instrument of partnership specifying the shares of partners,**
 - (b) it is registered with the Registrar of Firms within six months of its commencement;**
 - (c) any change in its constitution is evidenced by a new partnership deed, similarly registered with the Registrar of Firms;**
 - (d) none of the partners is a nominee or benamdar of any other; and**
 - (e) the return of income of the partnership is signed by all the partners.**
- (2) There should be a provision for the cancellation of recognition if the partnership is found to be a bogus one.**
- (3) The tax on a recognised firm may be fixed in such a manner that the rate of tax on a firm with a larger number of partners is higher than that on a firm with a smaller number.**

Tax on Income from House Property

10. Income from house property is determined on the basis of the annual value of the property consisting of any buildings or lands appurtenant thereto. Annual value is taken to be the sum for which the property might reasonably be expected to be let from year to year, subject to certain adjustment for municipal taxes. This concept borrowed from the UK. Income-tax law has sometimes led to unnecessary litigation because in theory, the determination of the annual value depends upon the subjective opinion of the Income-tax Officer. In actual practice, the Department, in a large number of cases, has been adopting the actual rentals received or the municipal valuation of the property, whichever is greater, as the basis of assessment. In the return prescribed under the Act, only these two amounts are mentioned. The Working Group has recommended that this practice can be given a statutory basis. We agree that the gross annual value of the property should be either the rentals receivable or the municipal valuation of the property whichever of the two is greater. From this amount, the full municipal tax (instead of half of it in regard to properties constructed after 1-4-1950) should be deducted. The latter part of the recommendation has already been implemented by appropriate amendment to Sec. 23 of the Income-tax Act effective from 1-4-1968 *vide* Finance Act of 1968.

Recommendation

11

We recommend :

The Income-Tax Act, may be amended so as to provide that the annual value of a house property is determined on the basis of the annual rentals received or receivable or the municipal valuation of the property whichever of the two is greater,

Provisional Assessment to be abolished

11. When returns are received, the Income-tax Officer is required, under the law, to make a provisional assessment. This provisional assessment is made after a scrutiny of the return and the documents filed therewith. With the introduction of the self-assessment scheme by which every assessee is required to pay the tax within a month of filing the return of income provided the tax payable on the basis of the return is Rs. 500 or more, the need for making a provisional assessment has largely disappeared. Further, the procedure relating to provisional assessment may lead to the defeat of the self-assessment provisions. Thus, when a provisional assessment is made just before the expiry of the period for the payment of the self-assessed tax, the assessee will automatically get a further extension of time of 35 days. We, therefore, agree with the suggestion of the Working Group that the provisions relating to provisional assessment should be deleted and self-assessment made compulsory for all cases where the tax payable is Rs. 100 or more. In such cases, the tax should be made statutorily payable along with the return or one week, at the most, after the submission of return instead of one month from the date of filing the return as obtaining at present.

Recommendation

12

We recommend :

The provisions relating to provisional assessment may be deleted and self-assessment made compulsory for all cases where the tax payable is Rs. 100 or more.

Tax Credit Certificates Scheme

12. A potent source of complexity in Income-tax law is the use made of it as an instrument for operating schemes of incentives for economic activities. A whole Chapter in the Income-tax Act, viz., Chapter XXII B beginning with Sec. 280Y and ending with Sec. 280ZE, is devoted to Tax Credit Certificates. These provisions seek to provide incentives for certain economic objectives, like increased production, greater exports, formation of new companies, expansion of existing industries and reducing the concentration of industry in metropolitan areas. Five schemes have so far been framed under the provisions of Chapter XXII B and the particulars of the Schemes together with the dates with effect from which they have come into being, are given below :—

<i>Scheme</i>	<i>Sec.</i>	<i>Date</i>
(1) Scheme to encourage exports.	280ZC	1-10-1965
(2) Scheme to encourage production of certain goods liable to central excise duty.	280ZD	1-12-1965
(3) For providing incentive to individuals and Hindu Undivided Families to invest in newly floated equity shares of certain companies.	280Z	1-3-1966
(4) For enabling expansion of industry for companies engaged in more important industries.	280EB	1-11-1966
(5) For facilitating the shifting of industrial undertakings from urban areas.	280ZA	1-9-1967

13. The Working Group has remarked that the schemes framed under these sections are so complicated in their operation that the basic purpose of providing incentives for the lines of activity envisaged has been defeated.

14. The Working Group has observed as follows—

“If the Schemes were less complicated and better publicised, perhaps, the results would have been better. In our view, it is because they got merged in the Income-tax provisions, they suffered this fate, making the Income-tax Act, in the process, more complex.”

15. The nexus between the schemes mentioned above and the Income-tax is rather tenuous. Apart from the complicated nature of the provisions referred to by the Group, the administration of the Scheme casts additional burden upon the Department without any comparable advantage.

Recommendation

13

We recommend :

The disadvantage of introducing complexity in the Income-tax law and its administration should be set off against the possible advantages envisaged by the use of that law as an instrument for providing incentives to various schemes of development. Whenever the need for providing such an incentive arises, attempts should be made, as far as possible, to achieve the objective aimed at through methods other than the indirect one of providing some savings in income-tax.

CHAPTER VI

EVASION

The nature of the income-tax levy is such that the problem created by its evasion by those who have incomes from sources such as business is a particularly difficult one to solve. The subject matter of taxation, namely, "income", arises in those cases from transactions which by their very nature are not within the ken of the assessing authority at the time when he attempts to make an assessment. For an unscrupulous assessee, various methods are available for suppressing transactions which had produced his income and the assessing authority who has to tackle the cases of such persons is like one groping in the dark.

2. The problem needs to be attacked on two fronts. Institutional arrangements should be put through for gathering as much information as possible from external sources about the financial transactions of assessees. The information so obtained can be used for checking the correctness of the incomes shown by the assessees in their returns and for enhancing them, where necessary—of course, after giving the assessees an opportunity of being heard. In addition to the widening of the horizon of information which will be useful for making assessments, it will be necessary to provide for severe punitive action against those who have been found to evade taxes. The law has recently been amended to provide for more stringent penal action than what was permissible in the past. As regards the arrangements for collecting information, we will touch upon those which are already in existence and indicate the improvements which are necessary. We will also suggest amendments to law which will help the Income-tax Department in its attempts to deal with the problem of evasion.

3. The sources of information which may lead to the discovery of new assessees or will be relevant to the assessment of those already on the books of the Department may be grouped into three categories :

4. (i) Government agencies outside the Income-tax Department which have dealings with the general public. The following are examples :

- (a) Departments making disbursements on a large scale to contractors and suppliers of goods, *e.g.*, Railways, Defence and Supply Departments and the Public Works Departments;
- (b) Registrars' Offices where the transfer of immovable properties are registered;
- (c) Municipalities which have a record of properties built from time to time;
- (d) Sales Tax Department which will have information regarding turn-over of their assessees;
- (e) Chief Controller of Imports & Exports who has details about import licences granted.

(ii) Details which can be obtained from non-Government agencies
Examples are :

- (a) Information furnished by companies under Section 186 of the Income-tax Act in respect of dividends exceeding Rs. 5,000 paid to non-corporate shareholders;
- (b) Information furnished by contractors under Section 285A of the Income-tax Act regarding contracts for the construction of buildings or supplies of goods or services for amounts exceeding Rs. 50,000.
- (c) Information furnished by banks about advances made or loans granted by them to their constituents on the security furnished by third parties;
- (d) Information received from financing companies regarding deposits made with them;
- (e) Information gathered by the Income-tax Officer while examining the accounts of an assessee about substantial payments made by him for the purchase of goods, payment of commission, brokerage etc.

(iii) Results of a physical survey of properties in a selected area including the eliciting of information from those residing or doing business therein.

5. The collection and dissemination to the concerned authorities of the information obtained from the first two sources is entrusted to the "Special Investigation Branches" in the various Commissioners' offices. It would appear that the attention paid to this work has not been adequate. Further, the information furnished is not made full use of. One of the reasons for the unsatisfactory working of the Special Investigation Branches is stated by the Group to be the saddling of these Branches with items of work not relevant to their main function. The position in this regard may be rectified by divesting Special Investigation Branches of other items of work. Further, there does not appear to be an adequate supervision of the work of the Branches and checking of the utilisation of the information made available by them. The third reason may be the inadequacy of manpower. We attach great importance to the successful working of these Branches. Their working should be reviewed immediately and any needed addition to staff should be provided. We have elsewhere recommended that the Internal Audit Department of the Commissioner should be placed in the charge of an Inspecting Assistant Commissioner. This officer may also be in charge of the Special Investigation Branch. He should continuously keep himself informed about the progress of the work of the Branch as well as of the utilisation of the information furnished by it as well as by such Branches in other Commissioners' charges. (The Special Investigation Branch in each Commissioner's charge should receive in the first instance relevant information from other Branches and then pass it on to the concerned assessing authorities.) Periodical inspections of the functioning of the Special Investigation Branches should be organised by one of the Directors of Inspection.

6. The third source of information usually called 'External Survey' which had been carried on for the past several years has now been suspended. We recommend that at a suitable time this may be revived, particularly in view

of the fact that we have recommended a quick method of disposal for small income cases of the type which is likely to be thrown upon on a large scale by the external survey.

Recommendation

14

We recommend :

- (1) (a) **The Special Investigation Branches in the Commissioners' charges should be strengthened.**
- (b) **They should concentrate on collection and dissemination of information relevant for purposes of assessment and their energies should not be directed to other items of work.**
- (c) **They should be placed under the immediate supervision of an Inspecting Assistant Commissioner who will also be in charge of Internal Audit Department.**
- (d) **Periodical Inspection of their work should be organised by one of the Directors of Inspection.**
- (2) **External Survey, which has been suspended, may be revived at a suitable time.**

Legislative Measures

7. The Working Group has suggested the following legislative measures for dealing with the problem of tax evasion.

(a) The Income-tax rules and the Wealth Tax rules may be amended to compel a person to enter in his return the particulars of the assets; or sources of income beneficially held for him by others. It should also be provided in law that unless such holdings are declared for the purposes of income-tax and wealth-tax, no claim to them will be enforceable under the general law.

(b) The law may be amended so as to club the income of husband and wife and treat the combined income as one unit.

(c) Whenever a tax payer submits accounts to the Income-tax Officer in support of a return made by him, the supporting accounts should be deemed as a part of the return for the purposes of the penalty provisions of the Income-tax Act. Every return should bear a verification certificate affirming the accuracy and the truth of the transactions entered in the accounts on which the return is based. Further, the certificate should include two positive statements, namely :

- (i) that all cash takings have been recorded in the books and that no cash has been held outside the books, and
- (ii) that all stock has been included in the stock figures valued at cost or market value (whichever is the method regularly adopted by the assessee) and that no stock is held outside the accounts.

(d) As a considerable amount of black money is introduced through indigenous bankers and hundi brokers, legislation may provide that no indigenous banker or hundi broker or a person other than a bank engaged in money lending business should possess a closing cash balance in his book

exceeding Rs. 20,000/-. Every payment made or amount received by him in excess of Rs. 10,000 should be by way of a crossed "Account Payee" cheque on a scheduled bank. It should further be provided that such a person should not hold cash exceeding Rs. 5,000 outside the accounts.

(e) In all other cases, the limit of holding cash in the account books should be raised to Rs. 50,000/- which should be sufficient for day to day purchases and if any excess amount is required, it should be drawn from the bank and intimation of this should be sent to the Income-tax Officer.

(f) It is necessary to have the assistance of expert valuers for purposes of valuing property transactions. These valuers should be employed by the Central Board of Direct Taxes with zonal offices in Bombay, Calcutta, Delhi and Madras and should offer expert assistance to the Income-tax Officers whenever any question of under-assessment of property value arises. If, on the basis of the expert advice, it is clear that there has been an understatement, the law should enable the Tax authorities to challenge the valuation in the same way as the Registrar is enabled to do for the purposes of the Stamp Act.

(g) While making the wealth-tax return, the assessee should be compelled to give the detailed items of jewellery instead of lump figure as at present and that no transaction of purchase and sale of jeweller exceeding Rs. 10,000 should be effected except through approved dealers of jewellery.

(h) It is desirable to make a provision in the Income-tax Act that agricultural income will be included in the total income of a person for the purpose of rate of tax chargeable on his total income excluding agricultural income.

8. The suggestion in (a) has been made with a view to countering attempts at concealing income or assets in the names of others. Transactions in which properties and assets are acquired by a person with his funds but in the names of other persons, are permitted by law and are common. It would not be practicable to impose an effective ban on such transactions. All that can be done is to make it risky for a person to conceal his income by investing it in the names of others. The suggestions made by the Working Group would appear to go a long way in compelling a person to disclose all his income and assets held by him in other names. We endorse them.

9. As regards the suggestion at (b), even under the existing law, the income of a wife from a firm in which her husband is a partner is clubbed with the income of the husband from that firm. We consider that it is not desirable to go beyond this and club the income of husband and wife for the purpose of income-tax under all circumstances. The Commission have no evidence that significant evasion has taken place because husband and wife are taxed separately on their incomes. The Commission therefore do not recommend this suggestion of the Working Group.

10. We endorse the proposal at (c).

11. As regards the suggestions (d) and (e), theoretically, the control of cash hoards could be used as a weapon in the fight against tax evasion. However, we do not think that it would be a practicable proposition to prescribe in all cases that the cash balance held in the books shall not exceed a stated figure. However, we endorse, in principle, the suggestion that persons engaged in money-lending business (other than

banking companies) should clearly indicate in the accounts of the business the money available for the business and keep in the banks all amounts in excess of a prescribed maximum. What this maximum should be, may be fixed by law, after taking all relevant factors into consideration. As regards the suggestion that the transactions in excess of Rs. 10,000 should be by way of a crossed cheque, we find that a variant of this suggestion has already been implemented by a provision in the Income-tax Act, 1961 as introduced by the Finance Act of 1968 to the effect that subject to certain exemptions, no payment exceeding Rs. 2,500 at a time would be permitted to be deducted as an admissible expenditure for purposes of computing income from business unless it is made by way of a crossed cheque or draft.

12. The suggestion made at (f), we are informed, has already been implemented to the extent that a central pool of valuers has been established with zonal offices in important centres. Therefore, the only part of the recommendation that remains to be implemented is to have a provision in the law to enable the Government to challenge a transfer in the same way as the Registrar is vested with powers to challenge a transaction under the Stamp Act. We support this suggestion.

13. The first part of the suggestion in (g), namely, amending the Wealth Tax return, has since been implemented by the Government. As regards the second part of the suggestion, viz., that restriction should be imposed in regard to purchase and sale of jewellery exceeding Rs. 10,000, from any one other than an approved jeweller, we are not convinced of its practicability.

14. As regards the suggestion at (h) that the law should be amended to include agricultural income in the total income for rate purposes, we appreciate its merits. However, we understand that this matter had already been examined by the Ministry of Law and that there are some constitutional difficulties.

Recommendation

15

We recommend :

- (1) (a) The Income-Tax and Wealth-tax returns may be so amended as to require an assessee to certify that they cover not only the source of income and assets held in his name but also those which are beneficially held for him by others.
- (b) Every return should bear a verification certificate affirming income and assets are declared for purposes of income-tax and wealth-tax by an assessee his claim to them will not be enforceable in law.
- (2) (a) When accounts are submitted by an assessee in support of the return made by him, those accounts should be deemed as a part of the return for the purposes of the penalty provisions of the Income-tax Act.
- (b) Every return should bear a verification certificate affirming the accuracy and the truth of the transactions entered in the accounts on which the return is based. The certificate should also include the two following statements viz.—

- (i) that all cash takings have been recorded in the books and that no cash has been held outside the books; and
 - (ii) that stock has been included in the stock figures valued at cost or the market value (whichever is the method regularly adopted by the assessee) and that no stock is held outside the accounts.
- (3) Persons engaged in money-lending business (other than banking companies) should clearly indicate in the accounts of the business the money available for the business and keep in the books all amounts in excess of a maximum to be prescribed by law.
- (4) Tax authorities (like the Registrar, for the purposes of Stamp Act) should be enabled by law to challenge valuation of immovable property if, on the basis of expert advice, it is found that property has been undervalued.

An all-India Register of Numbers

15. The Working Group is of the view that one of the major steps in preventing tax evasion is to provide for identification of assesseees and the transactions they enter into. This is to be achieved by introducing an all-India registration system. In para 6.19 of its report the Group has given an outline of a system of giving permanent numbers to assesseees. After the numbering is completed, a procedure should be devised and enforced through law for the quoting of the registered number in transactions involving capital transfers or mercantile or banking transactions exceeding in value a prescribed amount. This will facilitate the cross-verification of transactions. The same all-India registration number can be utilised in transactions with other Government Departments like Import Control, Public Works Department and the Railways.

16. The immediate effectiveness of an All-India Register of Numbers, as a weapon to be wielded against tax evasion may not be impressive. However, there is a case for maintaining an all-India numbering because it will facilitate compilation of statistics on a national scale and at a future date will prove to be a useful tool for gathering information. We, therefore, support the idea of an all-India registration number. The scheme will have to be carefully worked out because one hastily introduced will, if it is not fool-proof, result in more harm than good. Meanwhile, the suggestion that the income-tax numbers should be quoted in transactions of the type mentioned above can be implemented, the existing General Index numbers being used for the purpose.

Recommendation :

16

- (a) Steps may be taken to introduce a system of registration of assesseees in an all-India list on the lines of the scheme described in para 6.19 of the Report of the Working Group.
- (b) In the meanwhile, a procedure may be devised and enforced by law for the quoting of the existing General Index Numbers of assesseees in transactions involving substantial capital transactions or mercantile or banking transactions exceeding in value a prescribed amount.

17. We have made recommendations on institutional arrangements for collection of information relevant to assessment and for enacting certain legislative measures which will help the Department in its fight against evasion. There is also statutory provision for publishing the names of persons who have been penalised for tax offences. However, all these will not in themselves put an end to evasion. We have already mentioned how income-tax evasion is a particularly difficult problem to grapple with. It is so all over the world. But the Government in India have to create a climate of odium against tax evaders. With their extensive areas of patronage, rewards, and restrictions, memberships and invitations, they could make the tax-evader feel that he is a *persons non grata*.

CHAPTER VII

SOME ADMINISTRATIVE ISSUES

The Working Group has made a number of proposals on various administrative matters. We have selected the more important of them and have formulated our recommendations thereon.

Central Board of Direct Taxes :

2. The Working Group has suggested that the Central Board of Direct Taxes should be reconstituted as an independent executive authority, not concerning itself with policy. We are not in agreement with this suggestion. The Head of a Revenue Department is in the best position to advise the Government on policy and it would be unrealistic to exclude that authority from advising on policy. The Central Board of Direct Taxes as well as the Central Board of Excise and Customs, like their predecessor, the Central Board of Revenue, have been responsible for policy making in addition to being responsible for administering the Departments under them. This arrangement ensures that decisions of policy are taken only after considering all the administrative implications and also that implementation by the administration is in accordance with the policy of Government. It also makes for economy and speed in decision making at the top levels. We had in our report on "The Machinery of the Government of India and its procedures of work" pointed out that the Central Board of Direct Taxes and the Central Board of Excise and Customs "have a distinctive character of their own and combine policy-making with executive functions to the advantage of both". The Commission would, therefore, recommend that rather than be deprived of its policy making responsibilities, the Central Board of Direct Taxes should be allowed to function as a self-contained department administering not only its subordinate offices but also its headquarters establishment.

3. The Board now consists of a Chairman and four Members. The Working Group has suggested the constitution of a Board consisting of a Chairman and five Members. At the time when the Group made its proposal, the Board consisted of a Chairman and three Members. It has since been expanded and consists of a Chairman and four Members. We are by no means satisfied that the work-load justifies one additional member. All the work that is thrown up should be capable of being distributed between these five officers of high seniority. The Group has also proposed that on the Board being reconstituted with six Members, the three Directorates may be abolished. The field work done by the Directorates cannot be taken by the Board. We would, therefore, let the Directorates continue, but their number may be reduced to two and the work of all the Directorates may be redistributed between them.

Assistant Commissioners :

(a) Appellate Assistant Commissioners :

4. The Group has suggested that Appellate Assistant Commissioners should be given some training in judicial practice and procedure for a period of, say, three months by being attached to a District Judge. We are in favour of the Group's proposal. The period of training may, however,

be one month. It may be given to an officer on his first promotion as an Assistant Commissioner, as a preliminary to his posting as an Appellate Assistant Commissioner. The present policy of posting an officer as an Appellate Assistant Commissioner on promotion to the cadre of Assistant Commissioner has much to commend itself, as it gives a good change in the nature of duties of the promoted officer. We do not, therefore, suggest any change in this policy.

(b) *Inspecting Assistant Commissioners :*

5. The Group has suggested that Inspecting Assistant Commissioners should devote more time on pre-assessment advice and could be relieved of the inspection duties a good deal. It has also suggested that Inspecting Assistant Commissioners themselves should make assessment in big cases involving complicated points of law or intricacies in accounts. While we are in general agreement with the Group's proposal, we would not suggest the Inspecting Assistant Commissioners being relieved of all responsibility for post-assessment inspection. Pre-assessment guidance cannot be given in all cases. The more important of the cases in which pre-assessment advice is not given should be subject to a test-check by the Inspecting Assistant Commissioner. The system of internal audit and statutory audit makes it unnecessary for the Inspecting Assistant Commissioner to do a more detailed inspection than that suggested above. Internal audit should be strengthened and should be placed under an Inspecting Assistant Commissioner in each Commissioner's charge.

(c) *General :*

6. The cadre of Assistant Commissioners stands intermediate between the Income-tax Officer Class I and the Head of the Department and thus the position of the Assistant Commissioner is analogous to that of a Junior Administrative Officer in other Central Class I Services. Yet they are denied the pay scale available to such Junior Administrative Officers. The Assistant Commissioners draw pay in the scale of Rs. 1100—1600 whereas the Junior Administrative Officers get a scale of Rs. 1300—1600.

The Working Group has observed :

“..... we have no hesitation in stating that as compared to other Central Services, the officers in the Junior Administrative Grade in the Income-tax Department are called upon to discharge duties of a varied character from giving pre-assessment guidance to Income-tax Officers to planning searches and seizures, and settling cases involving considerable revenue. Besides, he has also a number of statutory duties to perform and we have suggested in this Chapter and in Chapter II that the Inspecting Assistant Commissioner should take over assessment powers in important cases. In administrative matters he acts as an effective Head of the Department and has control over a Range consisting of Income-tax Officers of both Class I and Class II. An Appellate Assistant Commissioner has powers of judicial review over all assessment without any monetary limit and occupies the same position as a District Judge, in this regard. The Law Commission in its 12th Report recommended an upward revision of the pay scale of the Appellate Assistant Commissioner and suggested that he

should be given a pay scale intermediate between the present scale and the scale of a Commissioner (Page 55, para 102 of Law Commission, 12th Report). We consider that this suggestion is eminently acceptable for the grade of Assistant Commissioners whether Inspecting or Appellate”.

We see merit in the argument that the Assistant Commissioners should not be treated differently from Junior Administrative Officers in other Central Services and accordingly recommend that they may be placed on the scale applicable to the Junior Administrative Officers.

(d) Income-tax Officers :

7. The primary assessing authorities are the Income-tax Officers. They are in Class I as well as Class II. Staffing of Class I is through direct recruitment as well as by promotion from Class II. During the past several years, the Class II used to be filled through the promotion of Inspectors. Recently, however, the Central Board of Direct Taxes has made arrangements for direct recruitment to Class II. We are not in favour of this move. Direct recruitment to junior posts at two levels, viz., Class I and Class II creates difficult administrative problems and also creates a cadre of officers in Class II many of whom may have to stagnate therein for a long time. We, therefore, agree with the Working Group that the Class II should be filled up entirely through promotion of Inspectors. We, however, do not agree with the Group that officers in Class II should not be given assessment work. They should be put on assessment work on comparatively simpler types of cases. The strength of the Class II cadre may, however, be reduced over a period of years.

8. The Working Group has suggested that in keeping with designations of Class I officers of the same rank in other Central Services, Income-tax Officers in Class I should be designated as Assistant Commissioners. Thus officers of the rank corresponding to Income-tax Officers Class I are designated as Assistant Accountant General in the Audit Department; as Assistant Collectors of Customs in the Customs Department and as Assistant Controller of Defence Accounts in the Defence Accounts Department. Apart from the need to adopt a designation similar to those in use in other Central Departments, there is also a need, according to the Working Group, to recognise a change in official life by prescribing a designation which would “announce” that change. The Group, therefore, suggests that Income-tax Officers Class I may be designated as Assistant Commissioners and that the Assistant Commissioners in their turn designated as Deputy Commissioners. We appreciate the reasoning behind the Group’s suggestions. However, we feel that the designation ‘Assistant Commissioner’ as applied to an Income-tax Officer is likely to lead to considerable confusion in the public mind. We would, therefore, suggest the designation of “Senior Income-tax Officer” for Income-tax Officers Class I.

Recommendation

17

We recommend :

- (1) (a) The Central Board of Direct Taxes should be allowed to function as a self-contained department of the Government administering not only its subordinate offices but also its headquarters offices.

- (b) One of the three posts of Director of Inspection may be abolished.
- (2) Income-tax Officers on promotion to the grade of Assistant Commissioners should be given training in judicial practice and procedure by being attached to a District Judge for a period of one month. This training will be a preliminary to his posting as Appellate Assistant Commissioner.
- (3) (a) With the introduction of internal as well as statutory audit, the inspections carried on by inspecting Assistant Commissioners may be restricted to the test-check of important cases of assessment in which pre-assessment advice has not been given by him.
- (b) Internal Audit may be placed under the direct supervision of the Inspecting Assistant Commissioner in each Commissioner's charge.
- (4) Assistant Commissioners should be placed in the same pay scale as that of Junior Administrative Officers in the Central Services.
- (5) In future, direct recruitment to Class II of Income-tax Officers should be stopped. The strength of the Class II cadre may be reduced over a period of years.
- (6) Income-tax Officers in Class I may be designated as Senior Income-tax Officers.

CHAPTER VIII

SUMMARY OF RECOMMENDATIONS

CHAPTER II—MEASURES TO EXPEDITE THE DISPOSAL OF ASSESSMENTS

1. (1) A system of prior agreement of the income-tax liability for the next three years based on the results of the last three assessments (or on the basis of the current assessment made on a new assessee) may be introduced for dealing with the cases of small shop-keepers, hawkers and vendors (who are not likely to maintain regular accounts) where annual income does not exceed Rs. 7,500/-
- (2) The law may be amended rendering it unnecessary to call the assessee for an interview if a small addition is made to the income declared in the return in order to rectify deficiencies. The maximum of addition that can be so made may be fixed by law.
- (3) The procedure for assessment in cases other than those mentioned in (1) may be simplified in the manner described in paragraphs 7 to 9.
- (4) The provisions of Rule 12A may be amended so as to provide for the furnishing of the following information in all cases in which the returned income from business exceeds Rs. 50,000 and the returns are prepared by Chartered Accountants :
 - (a) a brief history of the case;
 - (b) the nature of the business;
 - (c) the books of account maintained;
 - (d) the documents sent along with the return;
 - (e) the number of bank accounts maintained;
 - (f) brief explanation of the various loans and overdrafts appearing in the Balance sheet; and
 - (g) a brief explanation of the entries in the Capital account;

CHAPTER III—ARREARS OF COLLECTION

2. Appropriate amendment should be made in the Income-tax Act to provide that no appeal be entertained from an assessee unless the tax on the undisputed amount involved in the assessment is paid or satisfactory arrangements are made for the payment of such tax.
3. Action should be taken for expediting the write off of outstanding demands if they are found clearly to be irrecoverable. Such demands should be scrutinised by a committee consisting of the Commissioner the Inspecting Assistant Commissioner, and the Income-tax Officer concerned if the amount to be written off does not exceed Rs. 2 lakhs. Where such amount ranges between Rs. 2 lakhs and Rs. 5 lakhs, the committee for scrutinising should consist of the Commissioner

involved, the Commissioner and a Director of Inspection should scrutinise the cases and put them up to the Board for disposal.

4. Commissioners and Inspecting Assistant Commissioners should impress on the assessing officers that over-assessment would be noted as a defect indicating want of judgment and a sense of proportion.
5. (1) The recovery work should be taken over by the Income-tax Department in those charges where it is now entrusted to the States.
(2) (a) The Estate Duty Act may be amended so as to provide for recoveries on the lines provided in the Income-tax-Act.
(b) Provision may be made in the Estate Duty Act for the prevention of transfer, before payment of the relevant Estate Duty, of immovable property left by a deceased intestate.

CHAPTER IV—FACILITIES FOR TAX-PAYERS

6. Basic literature on tax-payers' obligations and rights should be brought out in Hindi, English and the regional languages.
7. The scheme regarding the opening of cash counters in Income-tax offices and the maintenance of Personal Ledger Accounts as suggested by the Working Group may be examined by the Government for being introduced in big cities like Bombay, Calcutta, Delhi, Madras, Kanpur, Bangalore, Ahmedabad and Hyderabad.

CHAPTER V—REMOVAL OF AVOIDABLE COMPLEXITIES IN THE LAW

8. (a) Amendments to tax laws should be made only after a careful survey of their total effect by all concerned. It will not be possible to make such a survey if amendments are rushed through the annual Finance Bill which needs to be passed before a prescribed date. Such amendments should therefore be made through separate Bills whose provisions can be considered in detail by select committees and on which the various professional or trade and industrial bodies will have an opportunity to express their considered views.
(b) Before rules are amended or new rules framed, the views of the Commissioners of Income-tax and of leading professional or trade and industrial bodies should be ascertained and considered.
9. A standard "previous year" should be prescribed for companies. This may be the calendar year if the financial year continues to commence on the 1st of April. However, if the financial year is to commence on the 1st of November as recommended by us in our report on "Finance, Accounts and Audit", the "previous year" for companies may be taken to be the year ending on the 30th of June.

10. (1) Partnership may be recognised for the purpose of income-tax assessment if—

- (a) it is evidenced by an instrument of partnership specifying the shares of partners;**
- (b) it is registered with the Registrar of Firms within six months of its commencement;**
- (c) any change in its constitution is evidenced by a new partnership deed, similarly registered with the Registrar of Firms;**
- (d) none of the partners is a nominee or benamdar of any other; and**
- (e) the return of income of the partnership is signed by all the partners.**

(2) There should be a provision for the cancellation of recognition if the partnership is found to be a bogus one.

(3) The tax on a recognised firm may be fixed in such a manner that the rate of tax on a firm with a larger number of partners is higher than that on a firm with a smaller number.

11. The Income-tax Act may be amended so as to provide that the annual value of a house property is determined on the basis of the annual rentals received or receivable or the municipal valuation of the property whichever of the two is greater.

12. The provisions relating to provisional assessment may be deleted and self-assessment made compulsory for all cases where the tax payable is Rs. 100 or more.

13. The disadvantage of introducing complexity in the Income-tax law and its administration should be set off against the possible advantages envisaged by the use of that law as an instrument for providing incentives to various schemes of development. Whenever the need for providing such an incentive arises, attempts should be made, as far as possible, to achieve the objective aimed at through methods other than the indirect one of providing some savings in income-tax.

14. (1) (a) The Special Investigation Branches in the Commissioners' charges should be strengthened.

(b) They should concentrate on collection and dissemination of information relevant for purposes of assessment and their energies should not be directed to other items of work.

(c) They should be placed under the immediate supervision of an Inspecting Assistant Commissioner who will also be in charge of Internal Audit Department.

(d) Periodical inspection of their work should be organised by one of the Directors of Inspection.

(2) External Survey, which has been suspended, may be revived at a suitable time.

15. (1) (a) The Income-tax and Wealth-tax returns may be so amended as to require an assessee to certify that they cover not

only the source of income and assets held in his name but also those which are beneficially held for him by others.

- (b) It should be provided by law that unless such sources of income and assets are declared for purposes of income-tax and wealth tax by an assessee his claim to them will not be enforceable in law.
- (2) (a) When accounts are submitted by an assessee in support of the return made by him, those accounts should be deemed as a part of the return for the purposes of the penalty provisions of the Income-tax Act.
 - (b) Every return should bear a verification certificate the accuracy and the truth of the transaction entered in the accounts on which the return is based. The certificate should also include the two following statements, viz.,
 - (i) that all cash takings have been recorded in the books and that no cash has been held outside the books; and
 - (ii) that stock has been included in the stock figures valued at cost or the market value (whichever is the method regularly adopted by the assessee) and that no stock is held outside the accounts.
 - (3) Persons engaged in money-lending business (other than banking companies) should clearly indicate in the accounts of the business the money available for the business and keep in the banks all amounts in excess of a maximum to be prescribed by law.
 - (4) Tax authorities (like the Registrar, for the purposes of Stamp Act) should be enabled by law to challenge valuation of immovable property if, on the basis of expert advice, it is found that property has been under-valued.
16. (a) Steps may be taken to introduce a system of registration of assesseees in an all-India list on the lines of the scheme described in para 6.19 of the Report of the Working Group.
- (b) In the meanwhile, a procedure may be devised and enforced by law for the quoting of the existing General Index Numbers of Assesseees in transactions involving substantial capital transactions or mercantile or banking transactions exceeding in value of prescribed amount.

CHAPTER VII—SOME ADMINISTRATION ISSUES

17. (1) (a) The Central Board of Direct Taxes should be allowed to function as a self-contained department of the Government administering not only its subordinate offices but also its headquarters offices.
- (b) One of the three posts of Director of Inspection may be abolished.
- (2) Income-tax Officers on promotion to the grade of Assistant Commissioners should be given training in judicial practice and

procedure by being attached to a District Judge for a period of one month. This training will be a preliminary to his posting as Appellate Assistant Commissioner.

- (3) (a) With the introduction of internal as well as statutory audit, the inspections carried on by Inspecting Assistant Commissioners may be restricted to the test-check of important cases of assessment in which pre-assessment advice has not been given by him.
- (b) Internal Audit may be placed under the direct supervision of the Inspecting Assistant Commissioner in each Commissioner's charge.
- (4) Assistant Commissioners should be placed in the same pay scale as that of Junior Administrative Officers in the Central Services.
- (5) In future, direct recruitment to Class II of Income-tax Officers should be stopped. The strength of the Class II cadre may be reduced over a period of years.
- (6) Income-tax Officers in Class-I may be designated as Senior Income-tax Officers.

Sd/-

K. Hanumanthaiya

Chairman

Sd/-

H. V. Kamath

Member

Sd/-

Debabrata Mookerjee

Member

Sd/-

T. N. Singh

Member

Sd/-

V. Shankar

Member

Sd/-

V. V. Chari
Secretary.
New Delhi,
January 6, 1969.

